82-1309

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

ROBERT C. BALDWIN, et al.,

Petitioners,

v.

ATHALIE DORIS JOY,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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February 4, 1983

QUESTIONS PRESENTED

1. WHETHER IN MAKING THE *ERIE RAILROAD CO. V. TOMPKINS* PREDICTION OF STATE LAW A COURT OF APPEALS CAN BASE ITS DETERMINATION ON A POLICY GROUND WITHOUT SUPPORT IN STATE STATUTES OR CASE LAW AND IN DIRECT CONFLICT WITH POLICIES ARTICULATED BY THIS COURT?

2. WHETHER IN MAKING THE *ERIE RAILROAD CO. V. TOMPKINS* PREDICTION OF STATE LAW A COURT OF APPEALS CAN REJECT A DISTRICT COURT'S CONSIDERED DETERMINATION OF APPLICABLE STATE LAW BASED UPON A MERE DISAGREEMENT WITH THE DISTRICT COURT?

PARTIES

The petitioners, Robert C. Baldwin, Herman K. Beach, Jr., Edward M. Bleser, Philip H. Burdett, Cameron Clark, Jr., Walter M. Goddard, Richard F. Gretsch, Harlan H. Griswold, William A. Haist, Jr., Edward E. Harrison, William C. Keator, Dr. Henry W. Littlefield, Hubert T. Mandeville, P. Douglas Martin, William R. Moody, Hoyt O. Perry, Jr., Willard E. Roberts, Charles E. Spencer, III, Harold P. Splain, Daniel F. Wheeler, and Robert H. Whitney were defendants and appellees below. The respondent was the plaintiff and appellant below. In addition to the petitioners, the defendants-appellees were: Charles T. Kellogg, Philip H. Sagarin, Citytrust, and Citytrust Bancorp, Inc. The remaining defendants are: Nelson L. North, Horace Merwin, Frederick R. Miller, E. Cortright Phillips, Norman Schaff, Jr., Reid C. Spencer, and Francis W. Stosse.

On Jauary 24, 1983, Citytrust and Citytrust Bancorp, Inc. filed a Petition for Writ of Certiorari to this Court in this case entitled *Citytrust and Citytrust Bancorp, Inc. v. Athalie Doris Joy*, Docket No. 82-1244.

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The petitioners respectfully pray that a writ of certiorari issue to review the judgment and opinion of the Second Circuit Court of Appeals entered in this proceeding.

OPINIONS BELOW

The opinion of the Court of Appeals reversing the judgment of the District Court for the District of Connecticut, appears at 692 F.2d 880 (1982) (Appendix A, *infra*, A-1 to A-42). The District Court opinion appears at 519 F. Supp. 1312 (1981) (Appendix B, *infra*, B-1 to B-30).

JURISDICTION

The judgment of the Court of Appeals for the Second Circuit was entered on November 4, 1982. A timely petition for rehearing with a suggestion for rehearing *en banc* was denied on December 17, 1982 (Appendix C) and this petition for certiorari was filed within 90 days of that date. This Court's jurisdiction is invoked under 28 U.S.C §1254(1).

STATUTORY PROVISIONS INVOLVED

Federal Rules of Civil Procedure

Fed. R. Civ. P. 23.1. (Appendix D)

State Statutes

Conn. Gen. Stat. §33-320a (Appendix E, *infra*, E-1 to E-5)

Conn. Gen. Stat. §52-572j (Appendix E, *infra*, E-5 to E-6)

STATEMENT OF THE CASE

This petition arises out of a shareholder derivative action instituted in the District of Connecticut on December 1, 1977 purportedly on behalf of Citytrust and its parent, Citytrust Bancorp, Inc. (collectively the "Corporations"). The suit is brought against numerous individuals, all of whom are past or present officers and/or directors of the Corporations. The plaintiff alleges that the defendants violated the National Bank Act, 12 U.S.C. §§21 *et seq.*, and breached their common law fiduciary duties, by extending a series of loans to a real estate development corporation. The Complaint alleges both diversity of citizenship and federal question jurisdiction.

On August 15, 1979, the boards of directors of the Corporations authorized the establishment of a Special Committee on Litigation (the "Committee"), to determine whether the prosecution of the derivative suit was in the best interests of the Corporations. On July 16, 1980, the Committee adopted a lengthy report which recommended that the suit be dismissed against twenty-three defendants, primarily outside directors of the Corporations. The Committee report also recommended that settlement be sought with regard to the remaining seven individual defendants.

After the plaintiff refused to withdraw her claims in accordance with the Committee's recommendation, the twenty-three defendants moved for summary judgment based on the report. Thereafter, the Corporations filed a similar motion for summary judgment. The District Court then afforded the plaintiff an opportunity to conduct discovery as to the scope of the Committee's investigation, the Committee's good faith and its independence. *Joy v. North*, 519 F. Supp. 1312, 1315 (D. Conn. 1981) (App. B-3). At the conclusion of discovery, upon the plaintiff's failure to raise a triable issue of fact as to the independence and good faith of the Committee or the thoroughness of its investigation,

the District Court rendered summary judgment in favor of the twenty-three defendants.

In accordance with the inquiry mandated by *Burks v. Lasker*, 441 U.S. 471, 477-78, 485 (1979), the District Court first found that Connecticut law permitted the termination of a shareholder derivative suit upon a business judgment determination by independent directors that continuation of such an action would be contrary to the best interests of the corporation on whose behalf it was brought. The District Court next determined that such Connecticut law was not inconsistent with the policies of the National Bank Act, 12 U.S.C. §§ 21 *et seq.*, the federal law upon which the derivative suit is, in part, based. The District Court held that the scope of judicial inquiry here was properly limited to a review of the Committee's independence, its good faith and the thoroughness of its investigation, and found that the Committee had met those criteria.

The Second Circuit Court of Appeals, in a lengthy 2-1 decision, reversed the District Court. *Joy v. North*, 692 F.2d 880 (2d Cir. 1982) (App. A-1 to A-42). The Court of Appeals, speaking through the Honorable Ralph K. Winter, with the Honorable James L. Oakes concurring, held that the District Court should have applied its own business judgment to review the merits of the Committee's decision. The Honorable Richard J. Cardamone dissented.

The majority's discussion of the purported state law basis for its holding relies solely on one entirely irrelevant case and two entirely irrelevant statutes. These references to Connecticut law are obvious window dressing designed to disguise the true basis of the holding: the majority's view that special litigation committees cannot be trusted to evaluate derivative actions against other directors in an unbiased manner. Since the majority does not trust the directors, it arrogates their role to the court and sets forth an intricate set of guidelines for the exercise of *a court's* business judgment. Then, without remanding for applica-

tion of the standards it has newly established, the majority exercises its own business judgment, based on an assumed set of facts never found by the District Court, and reaches a determination different from that of the Committee.

REASONS FOR GRANTING THE WRIT

1. THE DECISION BELOW RAISES THE SIGNIFICANT AND RECURRING PROBLEM OF THE PROPER APPLICATION OF THIS COURT'S RULING IN *ERIE RAILROAD CO. V. TOMPKINS* WHEN THERE IS NO STATE STATUTE OR CASE ON POINT

As Judge Cardamone points out in hs dissent, 692 F.2d at 900 (App. A-41), the Second Circuit once before expressed the view that disinterested directors could not be trusted to place the best interests of their corporation above those of their fellow directors. *See Lasker v. Burks*, 567 F. 2d 1208, 1212 (2d Cir. 1978). This Court made two points in reversing that decision. *See Burks v. Lasker*, 441 U.S. 471 (1979). First, it held that state law controls the issue in cases involving special litigation committees unless it conflicts with federal policy. Second, it taught that a director's lack of independence was not to be presumed. In the absence of a clear statutory or other policy statement by Congress to the contrary, this Court found no basis in the Investment Company Act of 1940, 15 U.S.C. §§ 80a-1 *et seq.* (ICA), the Investment Advisors Act of 1940, 15 U.S.C. §§ 80b-l *et seq.* (IAA), or anywhere else for an inference that the conflict of interest experienced by a defendant director applied *by force of human nature* to a non-defendant director.

The majority's opinion in this case rests precisely on the very presumption that this Court found inappropriate. The Second Circuit, having lost its bid in *Lasker v. Burks*, *supra*, to incorporate into federal law its belief that disinterested directors are incapable of making a truly independent decision, has now sought to resurrect that belief as an element of state law. It has done so by giving lip service to the standards set forth in *Erie Railroad Co. v. Tompkins*, 304 U.S. 64 (1938), and its progeny, but in substance substituting its own view of appropriate policy for a conscientious attempt to predict state law. In order to prevent the lowe

federal courts from treating the requirements of *Erie* as a mere form of words within which the federal courts are free to develop their own common law based on their own policy judgments, this Court should grant certiorari.

A. *The Erie Rule Is Clear.*

In *Burks v. Lasker*, 441 U.S. 741 (1979), this Court held that federal courts must apply state law in determining the authority of a committee of independent directors to discontinue a derivative suit under the ICA and the IAA. Such an inquiry is similarly required by the National Bank Act, as the Court of Appeals, 692 F.2d at 885 (App. A-9), and the District Court, 519 F. Supp. at 1318 (App. B-2), recognized. Once it is recognized that federal law requires reference to underlying substantive state law, the rules set forth in *Erie Railroad Co. v. Tompkins*, *supra*, and its progeny must be followed in determining whether a committee of independent directors has authority to discontinue a derivative suit as to some of the original defendants under the "business judgment rule."[1]

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1. Because federal jurisdiction in this case is based partly on diversity of citizenship, *Erie* applies directly to the state common law claims asserted in the Complaint.

Although *Burks* recognized that the ultimate "decision [on the ICA and IAA claims was] not controlled by *Erie R. Co. v. Tompkins*" because the underlying cause of action was based on federal law, 441 U.S. at 476, *Burks* clearly established that the federal court had a duty to determine the power of a director's committee under state law as a "threshold inquiry." 441 U.S. at 477-80. This threshold inquiry, which turns solely on a state law question and which was the only inquiry reached by the Court of Appeals in this case, cannot be answered other than by reference to the same rules for determining state law that apply when state law provides the ultimate rule of decision.

In *Commissioner v. Estate of Bosch*, 387 U.S. 456 (1967), this Court confronted a federal estate tax question which turned on a state rule of decision. In rejecting a claim that it was bound by a state trial court's ruling on the state law question, this Court reviewed *Erie* and its progeny and concluded:

Both the Court of Appeals, 692 F.2d at 885 (App. A-9), and the District Court, 519 F. Supp. at 1318 (App. B-8), recognized that no Connecticut court has yet passed on this issue. Under such circumstances, a federal court's duty under *Erie* has long been clear: it must "ascertain from all the available data what the state law is and apply it rather than . . . prescribe a different rule, however superior it may appear from the viewpoint of 'general law' and however much the state rule may have departed from prior decisions of the federal courts." *West v. A.T.&T.*, 311 U.S. 223, 237 (1940). *See, e.g., Lehman Brothers v. Schein*, 416 U.S. 386 (1974); *Huddleston v. Dwyer*, 322 U.S. 232, 236 (1944); 1A Moore, *Federal Practice*, ¶0.309[2], at 3317; Wright, *Law of Federal Courts*, §58, at 271 (3d Ed. 1976).

Just as the rule is clear, so is its rationale. *See, e.g., Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198 (1956). The goal of *Erie* is to prevent the creation of rules of decision on state law issues based on federal judges' views of an appropriate common law. *See Bernhardt v. Polygraphic Co. of America, supra*, 350 U.S. at 202-04; *West v. A.T.&T., supra*, 311 U.S. at 236.

Thus, under some conditions, federal authority may not be bound even by an intermediate state appellate court ruling. It follows here then, that when the application of a federal statute is involved, the decision of a state trial court as to an underlying issue of state law should *a fortiori* not be controlling. This is but an application of the rule of *Erie R. Co. v. Tompkins, supra*, where state law as announced by the highest court of the State is to be followed. This is not a diversity case but the same principle may be applied for the same reasons, *viz.*, the underlying substantive rule involved is based on state law and the State's highest court is the best authority on its own law. If there be no decision by that court then federal authorities must apply what they find to be the state law after giving "proper regard" to relevant rulings of other courts of the State. In this respect, it may be said to be, in effect, sitting as a state court. *Bernhardt v. Polygraphic Co.*, 350 U.S. 198 (1956). 387 U.S. at 465.

Since *Burks* and *Erie* require identical inquiries in the present case, the issues the present petition raises are described solely in the more familiar terms of *Erie*.

B. *The District Court Engaged In A Conscientious Effort To Ascertain Connecticut Law.*

In predicting how the Connecticut Supreme Court would rule, District Judge Eginton examined Connecticut statutory law on corporations, Connecticut case law, concepts of modern corporate law and other relevant authority. He traced the application of the "business judgment rule" in Connecticut from its earliest manifestation in *Pratt v. Pratt, Read & Co.*, 33 Conn. 446 (1866), to its modern recognition in case law, statutes and commentary on Connecticut corporate law. *See* 519 F. Supp. at 1316-18 (App. B-5 to B-8). This review revealed that the "business judgment rule" pervades the Connecticut law of corporations.

The District Court next inquired whether the scope of the rule "is sufficient to encompass a decision by disinterested directors to dismiss a pending derivative suit." 519 F. Supp. at 1318 (App. B-8). After finding that the language of Connecticut case law was expansive with regard to the business judgment rule, the Court concluded that the Connecticut Supreme Court would be influenced primarily by "the extensive weight of judicial authority in other jurisdictions, wherein courts have found that when state law embraces the business judgment rule, its scope includes a decision by a disinterested and independent committee of directors to terminate a derivative suit, subject to limited review of the committee's good faith and integrity."[2] 519 F. Supp. at 1318 (App. B-8) (citing *Gaines v. Haughton*, 645 F.2d 761 (9th Cir. 1981); *Clark v. Lomas & Nettleton Financial Corp.*, 625 F.2d 49 (5th Cir. 1980), *cert. denied*, 450 U.S. 1029 (1981); *Galef v. Alexander*, 615 F.2d 51 (2d Cir. 1980);

2. The Connecticut Supreme Court has indeed in recent years looked carefully to the weight of judicial authority in other jurisdictions with regard to emerging doctrines. *See, e.g., Page Motor Co. v. Baker*, 182 Conn. 484, 438 A.2d 739 (1980); *Sheets v. Teddy's Frosted Foods, Inc.*, 179 Conn. 471, 427 A.2d 385 (1980); *Hopson v. St. Mary's Hospital*, 176 Conn. 485, 408 A.2d 260 (1979).

Lewis v. Anderson, 615 F.2d 778 (9th Cir. 1979), *cert. denied*, 449 U.S. 869 (1980); *Abbey v. Control Data Corp.*, 603 F.2d 724 (8th Cir. 1979), *cert. denied*, 444 U.S. 1017 (1980); *Cramer v. GTE Corp.*, 582 F.2d 259 (3d Cir. 1978), *cert. denied*, 439 U.S. 1129 (1979); *Abramowitz v. Posner*, 513 F. Supp. 120 (S.D.N.Y. 1981), *aff'd*, 672 F.2d 1025 (2d Cir. 1982); *Genzer v. Cunningham*, 498 F. Supp. 682 (E.D. Mich. 1980); *Maldonado v. Flynn*, 485 F. Supp. 274 (S.D.N.Y. 1980), *modified*, 671 F.2d 729 (2d Cir. 1982); *Rosengarten v. I.T.&T. Corp.*, 466 F. Supp. 817 (S.D.N.Y. 1979); *Lewis v. Adams*, Civ. No. 77-266C (N.D. Okla. Nov. 15, 1979); *Gall v. Exxon Corp.*, 418 F. Supp. 508 (S.D.N.Y. 1976); *Maldonado v. Flynn*, 413 A.2d 1251 (Del. Ch. 1980), *rev'd sub nom. Zapata Corp. v. Maldonado*, 430 A.2d 779 (Del. 1981); *Auerbach v. Bennett*, 47 N.Y.2d 619, 419 N.Y.S.2d 920, 393 N.E.2d 994 (1979)).

C. *The Court of Appeals Gave Only Lip Service To The Requirements of* Erie.

The majority, in reversing the District Court, totally ignored the Connecticut authorities relied on below. In holding that Connecticut would require a court to apply its own business judgment to second guess a special litigation committee, it nominally advanced two arguments. First, it asserted that such committees simply cannot be trusted to act independently. The essence of this belief appears in the following passage:

> As a practical matter, new board members are selected by incumbents. The reality is, therefore, that special litigation committees created to evaluate the merits of certain litigation are appointed by the defendants to that litigation. It is not cynical to expect that such committees will tend to view derivative actions against the other directors with skepticism. Indeed, if the involved directors expected any result other than a recommendation of termination at least as to them, they would probably never establish the committee. The conflict of interest which renders the business judgment

> rule inapplicable in the case of directors who are defendants is hardly eliminated by the creation of a special litigation committee.

692 F.2d at 888 (App. A-16). The District Court made no finding warranting any of these assertions. The record offers no support for them. They are merely the beliefs of the majority.[3]

Second, the majority contended that restricting judicial review to the Committee's bona fides would undermine the sole method — shareholder derivative suits — of enforcing the fiduciary obligations of directors and officers. Seen clearly, this contention is merely a restatement of the majority's central tenet. Unless it is assumed that a directors' committee cannot act independently and in good faith, there is no reason for believing that the fiduciary obligations of the directors and officers will not be enforced. *See Joy v. North*, *supra*, 692 F.2d at 900 (Cardamone, J., dissenting) (App. A-41).

While ignoring the authorities relied upon below, the majority attempted to tie its view of correct policy to Connecticut law by citing two statutes and one case. The transparent irrelevancy of these citations to the issue involved exposes the majority's decision for what it is: a bald statement of its own view of correct policy.

The majority's nod to state law consists primarily of the following passage.

> We detect no signals that Connecticut law is moving away from the enforcement of directors' and officers'

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3. In rejecting the Second Circuit's previous attempt to effectuate its view that disinterested directors cannot be truly disinterested, this Court made clear that lack of impartiality is a factual, not a legal, issue.

> While lack of impartiality may or may not be true as a matter of fact in individual cases, it is not a conclusion of law required by the ICA.

Burks v. Lasker, *supra*, 441 U.S. at 485 n.15.

> traditional fiduciary obligations. Connecticut legislation governing indemnification of directors and officers for expenses incurred in litigation supports the view we take here. Conn. Gen. Stat. Ann. §33-320a(b) (West 1982). Although that provision has no direct application to this case, attitudes toward indemnification are relevant to the issue before us. By its terms, the Connecticut statute is exclusive and cannot be varied by corporate by-laws. It calls for indemnification without court approval only in circumstances in which the defendant directors and officers secure a judgment in their favor. This legislation adopts the middle ground between no indemnification and permissible indemnification without regard to outcome and thus does not bespeak a negative attitude toward enforcement of fiduciary obligations through meritorious derivative litigation.

692 F.2d at 889 (App. A-19).

The indemnification statute relied upon by the majority is simply not instructive on the issue presented. It was never briefed or argued by either party in the courts below. No statute in any state grants the unbounded indemnification that the majority would apparently require to rule that state law permits dismissal of a derivative suit based on the business judgment of a committee of independent directors. Moreover, an examination of the court decisions that have addressed this issue uncovers no ruling based on a state indemnification statute. The reason is simple: not only does the indemnification statute have "no direct application" to the issue in this case as the Court of Appeals recognized, 692 F.2d at 889 (App. A-19), but any indirect application it has is tenuous at best.[4]

The majority also appears to rely on Connecticut General Statutes §52-572j. Section 52-572j is the state counterpart

4. Indeed, while the indemnification statute does limit a corporation's power to indemnify directors and officers directly, it grants unbounded discretion to a corporation to insure its officers and directors from any and all liabilities *at the corporation's expense*. Conn. Gen. Stat. §33-320a(f). *See* Cross, Connecticut Law of Corporations 309, 312-13 (1972).

to Fed. R. Civ. P. 23.1. The majority cites this provision for the proposition that plaintiffs have a virtually absolute right to prosecute derivative suits "subject to judicial findings of adequate representation of shareholders and approval of settlements." 692 F.2d at 889 (App. A-18).

However, as the District Court here observed, 519 F. Supp. at 1319 (App. B-11 to B-12), even a cursory review of the text of this statute reveals a legislative intent merely to provide a procedural mechanism by which a shareholder may bring a derivative action on behalf of the corporation. When Fed. R. Civ. P. 23.1 was invoked as a ground to prohibit termination of a derivative action in similar circumstances, this Court rejected the argument. *Burks v. Lasker, supra*, 441 U.S. at 485-86 n.16. As it did with its presumption of bias on the part of special litigation committees, the majority ignored this Court's and the District Court's teachings in order to impose its own opinions as to policy. Indeed, to obscure the true basis for its holding, the majority ignores even its own observation that Section 52-572j "has no apparent substantive effect." 692 F.2d at 890 (App. A-21). Nothing in either Rule 23.1 or Section 52-572j elevates them from the procedural mechanisms they are to the absolute rules restricting the corporate response to derivative suits that the majority would have them be.

The majority cites a single Connecticut case to support its view of that state's law. *Ferris v. Polycast Technology Corp.*, 180 Conn. 199, 208-09, 429 A.2d 850, 854 (1980). It cites *Ferris* for the proposition that courts have traditionally scrutinized the underlying fairness of corporate decisions benefitting directors. 692 F.2d at 888 (App. A-17). In *Ferris*, however, the Connecticut Supreme Court was concerned with personal self-dealing between a director and his corporation. *Ferris v. Polycast Technology Corp., supra*, 180 Conn. at 208, 429 A.2d at 854. Judicial scrutiny of directors' actions in this context is indeed traditional.

To assume, as the majority did by its citation of *Ferris*, that the creation of a special litigation committee is a self-dealing exercise is merely to express in different words a belief in the incapacity of special litigation committees to exercise unbiased judgment. To assume self-dealing is again to posit in contravention of *Burks v. Lasker, supra*, that as a matter of law special litigation committees are inherently untrustworthy.

The authority marshalled by the appellate panel ostensibly to ground its decision in state law collapses of its own irrelevancy. An *Erie* prediction is not made. It is given only lip service. Moreover, as the dissent points out, the majority's decision adopts a set of guidelines for trial courts which is "so complicated, indefinite and subject to judicial caprice as to be unworkable." 692 F.2d at 898 (Cardamone, J., dissenting) (App. A-37). No Connecticut court has ever assumed that it can or should make the business judgments the majority decision requires.[5]

Moreover, in its haste to effectuate its policy opinions, the Court of Appeals robbed the District Court of its proper role as factfinder and the defendants of their right to present evidence. In spite of the absence of any facts found by the District Court regarding the merits of the plaintiff's case or the persuasiveness of the Committee's report, the majority found that the plaintiff's probability of success in the derivative action was "rather high" and that the recovery will "far [exceed] the potential cost of the litigation."

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5. The deference of Connecticut courts to the business judgment of corporate directors is well-stated in *Edson v. Griffin Hospital*, 21 Conn. Supp. 55, 59, 144 A.2d 341, 344 (Super. Ct. 1958):

> It is a fundamental and generally accepted rule that courts will not interfere with the internal management of a private corporation. Questions of policy and management are left solely to the honest decisions of the officers and directors, and the court is without authority to substitute its judgment for theirs.

See also VanTassel v. Spring Perch Co., 113 Conn. 636, 645, 155 A.2d 832, 835 (1931). *Pratt v. Pratt, Read & Co.*, 33 Conn. 446, 459 (1866).

692 F.2d at 896-97 (App. A-33 to A-34). When the petitioners suggested in their Petition for Rehearing to the Court of Appeals the propriety of a remand for purposes of an evidentiary hearing and factfinding, the majority refused to change its decision. The majority's elaborate guidelines, its unwarranted factfinding, and its speculative conclusions are simply additional proof that its goal was to set policy, not to make an accurate prediction of Connecticut law.

D. *There Is A Need For This Court To Police The Application of* Erie.

Despite the clarity of the federal courts' duty in making the "*Erie* prediction," fulfilling that duty remains problematic because of the lack of clear signposts to the propensities of a state's highest court. The temptation constantly exists for a federal court, while perhaps using language indicative of adherence to the *Erie* rule, to substitute its own determination of relevant policy for a conscientious prediction of how the state's highest court would decide the question presented. The Second Circuit majority yielded to that temptation in this case.

This Court has recognized the need to exercise its certiorari jurisdiction to police *Erie's* application. *See, e.g., Lehman Brothers v. Schein*, 416 U.S. 386 (1974); *Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198 (1956); *King v. Order of United Commercial Travelers*, 333 U.S. 153 (1948); *Stoner v. New York Life Insurance Co.*, 311 U.S. 464 (1940); *West v. A.T.&T.*, 311 U.S. 223 (1940); *Six Companies v. Joint Highway District No. 13*, 311 U.S. 180 (1940); *Fidelity Union Trust Co. v. Field*, 311 U.S. 169 (1940).[6] As the

6. Certiorari jurisdiction has also been used to police the application of the similarly difficult-to-apply *International Shoe Co. v. Washington*, 326 U.S. 310 (1945), "minimum contacts" test for the exercise of personal jurisdiction. This Court has seen fit periodically to exercise its certiorari jurisdiction to review the application of the test to particular fact situations, even where there has been no showing that the particular fact situation is likely to recur. *See, e.g., Kulko v. Superior Court*,

majority's opinion in this case reveals, without this Court's active supervision, the lower courts will be too readily tempted to develop federal common law based on individual judges' views of appropriate policy to "fill the gaps" when the controlling state rule of decision has not been definitively announced by the state's highest court. Adherence to *Erie* becomes nominal only.

If the lower courts do not treat the process of determining state law differently from that of creating federal common law, the important principle of *Erie* will be effectively abandoned. The Court of Appeals ignored the distinction in this case. This Court should grant certioriari to prevent other lower courts from succumbing to the same temptation.

2. THE DECISION BELOW IS IN CONFLICT WITH DECISIONS IN OTHER CIRCUITS ON THE STANDARD BY WHICH DISTRICT COURT RULINGS ON STATE LAW ARE TO BE REVIEWED.

A. *All Other Circuits That Have Addressed The Issue Agree That The District Court's Determination Of The Law Of The State In Which It Is Located Is Entitled To Great Deference.*

Every circuit that has addressed the issue has held that the determination by a district court of the law of the state in which it sits is entitled to great deference on review by a court of appeals. *See, e.g., Garcia v. Friesecke*, 597 F.2d 284, 295 (1st Cir.), *cert. denied*, 444 U.S. 940 (1979); *United States v. Burnsed*, 556 F.2d 882, 884 (4th Cir. 1977), *cert. denied*, 434 U.S. 1077 (1978); *Robertshaw Controls Co. v. Pre-Engineered Products Co.*, 669 F.2d 298, 300 (5th Cir. 1982); *Bagwell v. Canal Insurance Co.*, 663 F.2d 710, 712

436 U.S. 84 (1978). In *Kulko*, the parties and lower courts were in agreement as to the proper rule to be applied to determine the propriety of the state court's exercise of jurisdiction over the defendant. The dispute was merely over the correct result in the particular factual setting involved.

(6th Cir. 1981); *White v. United States*, 680 F.2d 1156, 1161 (7th Cir. 1982); *Orlando v. Alamo*, 646 F.2d 1288, 1289-90 (8th Cir. 1981); *Walgreen Arizona Drug Co. v. Levitt*, 670 F.2d 860, 863 (9th Cir. 1982); *Loveridge v. Dreagoux*, 678 F.2d 870, 877 (10th Cir. 1982). Until its decision in the instant case, the Second Circuit appeared to be in accord with this view. *Lomartira v. American Automobile Insurance Co.*, 371 F.2d 550, 554 (2d Cir. 1967). However, the majority's rejection of the District Court's careful analysis of Connecticut law and the denial of rehearing *en banc* reveal that the Second Circuit no longer agrees that a district court's determination of the law of the state in which it sits should receive special deference from the appellate court.

This Court has stated that it will not overrule determinations of state law by federal courts skilled in the law of the states in which they sit unless the lower courts' holdings "are shown to be unreasonable." *Propper v. Clark*, 337 U.S. 472, 486-87 (1949). *See also United States v. Kimbell Foods, Inc.*, 440 U.S. 715, 740 (1979); *Butner v. United States*, 440 U.S. 48, 58 (1979); *Bishop v. Wood*, 426 U.S. 341, 345-46 (1976); *United States v. Durham Lumber Co.*, 363 U.S. 522, 526-27 (1960); *Township of Hillsborough v. Cromwell*, 326 U.S. 620, 629-30 (1946); *Huddleston v. Dwyer*, 322 U.S. 232, 237 (1944). This Court has not, however, ruled on the question whether a court of appeals must accord the same weight to a determination of home-state law by a district court. This case thus presents a significant question affecting the relations among the lower federal courts. *See King v. Order of United Commercial Travelers*, *supra*, 333 U.S. at 159.

As all the courts of appeals that have explicitly addressed this issue have concluded, the rationale supporting this Court's deference to lower federal courts on questions of local state law also supports similar deference by the courts of appeals to the district courts: a judge who sits in a partic-

ular state is in the best position accurately to predict how that state's courts would decide a question of state law. Circuit judges are drawn from all of the several states and territories contained in their circuits. This fact operates, as the Second Circuit itself once recognized, so that "[n]ot infrequently, no member of the panel of a court of appeals is a member of the bar of the state whose law is in question." *Lomartira v. American Automobile Insurance Co.*, *supra*, 371 F.2d at 554 n.6.

The majority in this case made no finding that the District Court's prediction of Connecticut law was "clearly erroneous," *e.g.*, *Harris v. Hercules, Inc.*, 455 F.2d 267, 269 (8th Cir. 1972). Nor is there any indication that the majority accorded the District Court's judgment on state law "special deference," *e.g.*, *Robertshaw Controls Co. v. Pre-Engineered Products Co.*, *supra*, 669 F.2d at 300, or "great weight," *e.g.*, *White v. United States*, *supra*, 680 F.2d at 1162. Indeed, the majority opinion makes no attempt to disguise that its holding is based on a simple disagreement with the District Court. The majority opinion never directly addresses the particulars of the District Court's reasoning. The appellate panel does not challenge the District Court's reading of Connecticut statutory and decisional law nor does it identify any errors in the reasoning of the District Court. Rather, the majority opinion merely recites what it sees as relevant policy considerations and concludes that these considerations counsel against reliance on the business judgment of independent directors.

This Court should grant certiorari to resolve the conflict between the Second Circuit and all other circuits that have addressed the question of appropriate deference to a district court's determination of an unsettled issue of state law. By so doing, this Court would both assure the use of uniform standards of appellate review within the federal judicial system and remind all lower courts that their obligation to predict state law in accordance with the holding in *Erie* is to be taken seriously.

CONCLUSION

For the foregoing reasons, a writ of certiorari should issue to review the judgment and opinion of the Court of Appeals for the Second Circuit.

Respectfully submitted,

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